

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #02-11**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Application of Tennessee's sales and use tax to purchases of materials which a contractor will use in building an addition to a church sanctuary.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed:

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification by the Commissioner shall be effective retroactively unless the following conditions are met, in which case, the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[NAME OF CHURCH] is a religious organization with property located in [CITY], Tennessee. The Church, as a local affiliate of a national church organization, has received a ruling from the Internal Revenue Service that it is exempt from federal income tax under Internal Revenue Code Section 501(c)(3).

It has also received an exemption certificate from the Tennessee Commissioner of Revenue to make purchases of tangible personal property or taxable services for its own use and consumption or to be given away (pursuant to Tenn. Code Ann. Section 67-6-322) without the payment of sales or use tax.

The Church plans to have an addition to its sanctuary built by a contractor. The purchase and installation of carpeting was part of the contractor's bid to construct the addition.

The new addition will have classrooms, restrooms, a kitchen and a multi-purpose room. The Multi-Purpose Facility¹ will be connected to the existing sanctuary by an enclosed gathering area.

The Church has no intention to use any part of the building addition for any revenue-generating purpose.

The Church currently has a local property tax exemption from the local county property tax assessor for its church property located in [CITY], Tennessee. The Church has received a letter from the assessor indicating that, once the proposed new addition to the building is completed and exemption forms are properly filed, he sees no reason why the new building will not also be exempt from local property taxes.

ISSUES

1. Will the new addition and the Multi-Purpose Facility be considered to be under the same roof as the church sanctuary and be considered church construction under the use tax exemption law?
2. If the contractor retained by the Church purchases the materials to be used in the construction of the addition and the Multi-Purpose Facility, is the contractor or the Church required to pay sales or use tax on the building materials?
3. If the Church purchases the building materials that the contractor will be using on the construction of the addition and the Multi-Purpose Facility, is the Church required to pay sales tax on the building materials?

¹ The Church has provided a copy of the Concept Design Proposal to illustrate how the Multi-Purpose Facility will be connected to the existing church sanctuary.

4. If carpet is installed in the new addition to the church sanctuary, is the Church required to pay sales tax on the carpet materials or installation of the carpet?

RULINGS

1. The new addition and the Multi-Purpose Facility, which will be added to and connected to the current sanctuary of the Church, will be considered church construction under the Tennessee Sales and Use Tax laws.²
2. The contractor is required to pay sales or use tax on materials it purchases and then uses for construction of the addition and the Multi-Purpose Facility for the Church. The Church is not liable for sales or use tax since it holds a current exemption certificate from the Commissioner of Revenue.
3. No.
4. No.

ANALYSIS

1. The new addition and the Multi-Purpose Facility proposed to be constructed for the [NAME OF CHURCH] will be connected to the current church sanctuary.³

However, the critical question for sales and use tax purposes is whether the addition and the Multi-Purpose Facility can be considered “church construction” as used in the use tax exemption provided under Tenn. Code Ann. Section 67-6-209(b).

The Department has typically looked at several aspects of a building being constructed by or on behalf of a church to determine whether it qualifies as church construction under this statute.

- (1) Does it qualify for exemption from property taxes?
- (2) Will it not be used for commercial purposes? and
- (3) Will it be used for commonly recognized church functions?

If these questions are each answered affirmatively with respect to particular construction, the Department has concluded the building is “church construction” under Tenn. Code Ann. Section 67-6-209(b).

² It should be noted that a construction project or a building constructed for a church need not be physically connected to a church’s sanctuary to qualify as “church construction” under the Tennessee Sales and Use tax laws.

³ See footnote 2 above.

Tenn. Code Ann. Section 67-5-212(a)(1) generally exempts from property tax the real property owned by a religious institution which is occupied and used by such institution purely and exclusively for carrying out one or more purposes for which the institution was created.

It is presumed that the first question can be answered in the affirmative based on the facts presented. Each part of the new addition and Multi-Purpose Facility – the classrooms, the restrooms, the kitchen, the multi-purpose room and the gathering room connector – apparently will be used for carrying out one or more purposes for which the Church was created and thus should qualify for a local property tax exemption.⁴

The second question also appears to be able to be answered affirmatively. Since the facts state that the new addition and the Multi-Purpose Facility will not be used for any revenue-generating purposes, there is no commercial purpose that would weigh against the Department’s determination that the building would constitute church construction.

Finally, the third question can also be answered in the affirmative. Church use of the addition for purposes of classrooms, restrooms, a kitchen, a multi-purpose room and a gathering area are all uses which are commonly recognized as church functions.

Therefore, the new addition and Multi-Purpose Facility constitutes “church construction” under Tenn. Code Ann. Section 67-6-209(b).

2. A limited exemption for a contractor to use materials for church construction without the payment of use tax on the materials is afforded by Tenn. Code Ann. Section 67-6-209(b). That statute provides, in applicable part, as follows:

Where a contractor . . . uses tangible personal property in the performance of the contract . . . , **except where the title holder is a church, . . . and the tangible personal property is for church . . . construction**, such contractor or subcontractor shall pay a tax at the rate prescribed by § 67-6-203 measured by the purchase price of such property . . . (Emphasis added. Tenn. Code Ann. Section 67-6-209(b).)

If the contractor retained by the Church purchases the materials to be used in the construction of the Church’s addition and Multi-Purpose Facility, retaining title to such materials as construction progresses, the contractor would be liable for sales tax (since it could not purchase the materials on a resale certificate) or for a use

⁴The Church has done all it can do at this point to confirm that a local property tax exemption will be granted by obtaining a letter of assurance from the local county property assessor. Nevertheless, it must be noted that any future official denial of the local property tax exemption relative to the addition and the Multi-Purpose Facility would negate the ruling that the construction proposed here is church construction.

tax on its cost of materials used in the construction contract. See Tenn. Code Ann. Section 67-6-203(a). The contractor would not qualify for the limited tax exemption provided in Tenn. Code Ann. Section 67-6-209(b) since the Church would not be the title holder of the materials used in the project.

It should be also noted that, if Church's contractor purchases materials, then sells them to the Church (transferring title and possession) and finally uses the materials previously sold to the Church to construct the church addition, the contractor may not initially purchase such materials on a resale certificate. It must pay the sales tax on those materials because it may not take advantage of the exemption afforded by a resale certificate under Tennessee law.

Tenn. Code Ann. Section 67-6-209(c) provides in applicable part as follows:

. . . However, the transfer of tangible personal property by a contractor who contracts for the installation of such tangible personal property as an improvement to realty **does not constitute a sale**, except as provided in § 67-6-102(8), and the **contractor shall not be permitted on this basis to obtain the benefit of any exemptions** or reduced tax rates available to manufacturers under § 67-6-206 or § 67-6-102(24)(E) . . . (Emphasis added. Tenn. Code Ann. Section 67-6-209(c))

This statutory provision prevents the contractor's sale of materials to the Church from being considered a sale under the tax laws and thus the contractor could not purchase the materials on a resale certificate. However, if such were done, the contractor's subsequent use of the materials – title to which has already passed to the Church – would subject the contractor to a use tax on its cost of the materials purchased.

The Church would not be liable for a sales or use tax under the facts presented since it holds a current exemption certificate issued by the Commissioner of Revenue.

3. If the Church purchases the building materials that the contractor will be using on the construction of the addition and the Multi-Purpose Facility, the Church would not be liable for sales tax on such materials.

The Church should present its tax exemption certificate issued by the Commissioner of Revenue to the materials supplier to take advantage of the tax exemption.

The contractor would not be liable for use tax on the materials (it used for the church construction) that were owned by the Church as long as the contractor did not first buy the materials and then sell them to the Church. (This is explained more fully in the Analysis of Ruling 2.)

4. Tenn. Code Ann. Section 67-6-209(b) provides in part as follows:

. . . The sales or use tax levied by this chapter shall not apply to carpet installed for a church when the church is exempt from sales or use taxes under Section 67-6-322.

Since the facts indicate that carpet will be installed for a church and the church in this instance has received an exemption certificate from the Commissioner of Revenue, the sales and use tax levied by Title 67, Chapter 6 would not apply. The Church would have no sales tax liability.

It must be noted that the Church has also received a contractor's bid for construction of the addition to the sanctuary, which bid includes the purchase and installation of carpeting.

Under these facts, neither the sales tax nor the use tax would apply to the vendor's cost of carpet materials since the Church is exempt from the sales and use tax under the statute cited above. In this particular instance, it does not matter that the sale of the carpet materials was part of a single contract that included installation. The statutory exemption applies to both the carpet materials installed and the installation of carpet, regardless of what the contract includes.

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APPROVED: Ruth E. Johnson
Commissioner

DATE: 04-26-02